IN THE UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF IDAHO

IN RE	)	
	)	
ADRIAN THOMAS WENGERT and	)	**Case No. 99-00123**
LAURA K. WENGERT,	)	
f.k.a. LAURA K. REESE,	)	
	)	
Debtors.	)	
	)	
_____	)	
	)	**MEMORANDUM OF**
DECISION		
KOWALLIS & RICHARDS, INC.	)	**AND ORDER**
an Idaho Corporation,	)	
	)	
Plaintiff,	)	
	)	
v.	)	**Adversary No. 99-6044**
	)	
ADRIAN WENGERT,	)	
	)	
Defendant.	)	
	)	
_____	)	

Terry C. Copple, DAVISON, COPPLE, COPPLE, & COPPLE, Boise, Idaho, for Plaintiff.

Scott D. Hess, JONES, GLEDHILL, HESS, ANDREWS, FUHRMAN, BRADBURY & EIDEN, Boise, Idaho, for Defendant/Debtor.

On January 19, 1999, Adrian and Laura Wengert filed a voluntary petition for relief commencing this chapter 13 case. Their Schedule I disclosed that Mr. Wengert ("Wengert") was a "Facilities Manager" for All-West Corporation and had been so employed for one week at the time of filing.

On February 23, 1999, Kowallis & Richards, Inc. ("K&R"), Wengert's former employer, filed a complaint and a motion for temporary restraining order and preliminary injunction.[1] The motion is based upon the "Non-Competition Agreement" Wengert executed while employed by K&R. This Court took the motion for preliminary injunction under advisement following hearing, and by this Decision determines that the motion shall be denied.[2]

FACTS

K&R is a business located in Boise which sells industrial fasteners (a term encompassing nuts and bolts, and a variety of other fastening devices) and related material to construction and manufacturing companies.

Wengert worked for K&R from October 12, 1993 to July 31, 1998. He initially worked as a warehouseman but, in January 1996, was promoted to "Assistant Operations Manager." On October 25, 1996, Wengert executed the "Non-Competition Agreement" ("the Agreement") with K&R which is at the heart of this dispute. The Agreement recites consideration paid of $1,000.00, and Wengert has acknowledged receiving that payment.

Under the Agreement, Wengert promised, for the duration of his employment by K&R and for 18 calendar months from termination of that employment,

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[1] This action was originally brought in the District Court of the Fourth Judicial District of the State of Idaho, Ada County. Wengert removed the action to this Court. Plaintiff sought remand or abstention, which request was denied.

[2] This Decision constitutes the Court's findings of fact and conclusions of law in this contested matter. Rule 7052, 9014.

> not to directly or indirectly own, manage, operate, control, be employed by, participate in, or be connected in any manner with the ownership, management, operation of, or control of any fastener and tool business or any other business presently or hereafter conducted by Employer similar to the type of business now or hereafter conducted by Employer in the Idaho counties of Ada, Canyon, Elmore, Idaho, Payette and Washington and the Oregon counties of Baker and Malheur or any area in the future that Employer may have operations.

Wengert also agreed to not divulge confidential or proprietary information or records of K&R and to not contact K&R's employees in an attempt to entice them to leave employment. The Agreement provided for enforcement by both injunctive relief and action for damages.

In December 1996, within two months of signing the Agreement, Wengert was promoted to "Operations Manager," as part of the "management team" with Terry Kowallis, K&R's President, and Tracy Kowallis. In that position, he supervised warehousemen and other staff and was involved with reviewing bids and pricing. Wengert's supervisory duties included training warehousemen and over-the-counter sales staff.

On July 31, 1998, K&R terminated Wengert.[3] Terry Kowallis testified that he and Tracy Kowallis were not satisfied with Wengert's overall performance and progress, particularly in his dealing with subordinates as he moved from labor to management.[4]

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[3] The position held by Wengert was that of an "at will" employee.

[4] Numerous issues were raised, tried and argued concerning the nature of K&R's dissatisfaction with Wengert's performance, the at will nature of his employment, the terms and provisions of the K&R Employee Handbook including the anticipated use of "progressive discipline," and certain alleged problems with use of employee purchase accounts. Wengert argues that K&R's allegedly "unclean hands" prohibits equitable relief. Further, *Insurance Center, Inc. v. Taylor*, 94 Idaho 896, 898, 499 P.2d 1252, 1254 (1972), recognized that, where employers are found to have unfairly dealt with an employee, enforcement of a covenant not to compete would be inequitable. *Id.* (citing *Drong v. Coulthard*, 87 Idaho 486, 496, 394 P.2d 283, 289 (1964)

(continued...)

After his termination, Wengert was unemployed for a period of time, then obtained a position from September through January 15, 1999 with a business outside the fastener and tool industry. In January 1999, Wengert accepted a position with All-West Fasteners, Inc. ("All-West") as its "Boise Logistic Facilities Manager."

Until the last year, All-West serviced its Boise customers through its Seattle, Washington office and, in part, by a sales representative based in Spokane, Washington. In December 1998, All-West opened a Boise warehouse to provide "logistical support" for its Boise based customers. Those customers are primarily, if not totally, in the electronics industry. Though both All-West and K&R are in the "fastener and tool" business, they serve separate niches of that business insofar as the subject geographic area is concerned.

The Boise warehouse of All-West stores product until it is delivered to local customers. No retail sales are made from the Boise warehouse, nor is any other sales function performed from the Boise warehouse. There has been no ongoing sales outreach or intent to develop customers in competition with K&R, and no new Boise customers have been obtained since Wengert was hired. All-West contends it is not using any information Wengert may have obtained during his employment with K&R. All-West's policy instructs all employees hired from what might be characterized as "related" industries not to transfer or use information gained from their prior employment while employed by All-West.

All-West does appear under several categories in the Treasure Valley phone directories "Yellow Pages" where K&R also appears. However, phone inquiries are referred either to Seattle or to the Spokane sales representative.

In short, Wengert is a non-management level employee of All-West charged with delivering products and maintaining product inventory for several

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[4](...continued)
(where promise not to compete is ancillary to employment contract, injunction to enforce the promise will not be granted unless the result is equitable)). However, given the Court's findings and conclusions on the reasonableness and enforcability of the Agreement's scope of prohibited employment, it need not address these other issues.

large, pre-existing customers of All-West in the Boise area. He has no sales responsibility, no involvement in marketing or obtaining new clients for All-West, no access to All-West's pricing structures, and is not charged in any sense with developing business, in this geographic area or otherwise, in competition with K&R.

Nevertheless, K&R seeks to enforce the Agreement's provision that Wengert may not "be employed by . . . or be connected in any manner with . . . any fastener and tool business . . . ."

APPLICABLE LAW

A. Injunction

The Agreement itself provides that it may be enforced by way of injunctive relief. The burden which must be met by the proponent is well established.

> The traditional equitable criteria for granting preliminary injunctive relief are: (1) a strong likelihood of success on the merits; (2) the possibility of irreparable injury to the plaintiffs if injunctive relief is not granted; (3) a balance of hardships favoring the plaintiffs; and (4) advancement of the public interest. *Los Angeles Memorial Coliseum Commission v. National Football League,* 634 F.2d 1197, 1200 (9th Cir. 1980). A preliminary injunction is not a preliminary adjudication on the merits, but a device for preserving the status quo and preventing the irreparable loss of rights before judgment. *Sierra On-Line, Inc. v. Phoenix Software, Inc.,* 739 F.2d 1415, 1422 (9th Cir. 1984). "In this circuit, the moving party may meet its burden by demonstrating either (1) a combination of probable success on the merits and the possibility of irreparable injury or (2) that serious questions are raised and the balance of hardships tips in its favor." *Los Angeles Memorial Coliseum Commission,* 634 F.2d at 1201.

Barahona-Gomez v. Reno, 167 F.3d 1228, 1234-35 (9th Cir. 1999).

B. Noncompetition agreements

Covenants not to compete have been addressed in numerous Idaho decisions, including *McCandless v. Carpenter*, 123 Idaho 386, 848 P.2d 444 (Idaho Ct.App. 1993); *Insurance Associates Corp. v. Hansen*, 111 Idaho 206, 723 P.2d 190 (Idaho Ct.App. 1986); *Insurance Center, Inc. v. Taylor*, 94 Idaho 896, 499 P.2d 1252 (1972); *Drong v. Coulthard*, 87 Idaho 486, 394 P.2d 283 (1964); and *Marshall v. Covington*, 81 Idaho 199, 339 P.2d 504 (1959). The court stated in *McCandless* as follows:

> This Court has previously noted the general rule regarding restrictive covenants as stated in *Marshall v. Covington*, 81 Idaho 199, 203, 339 P.2d 504, 506 (1959), which is that they
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> > will be enforced when they are reasonable, as applied to the covenantor, the covenantee, and the general public; they are not against public policy, and any detriment to the public interest in the possible loss of the services of the covenantor is more than offset by the public benefit arising out of the preservation of the freedom of contract.
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> *Dick v. Geist*, 107 Idaho 931, 933, 693 P.2d 1133, 1135 ([Idaho] Ct.App. 1985) The general rule is that a noncompete agreement is enforceable if it is supported by consideration, ancillary to a lawful contract, [and] reasonable and consistent with public policy. 54 Am.Jur.2d Monopolies, Etc. §511 (1971). The Idaho Supreme Court has held that noncompete agreements are enforceable in a variety of contexts including the sale of a business, employment relationships, principal-agent relationship where agent forfeited commissions because of competitive activity, and the sale of a franchise. The Court has also held that certain noncompete agreements are unenforceable. *See Insurance Center, Inc. v. Taylor*, 94 Idaho 896, 499 P.2d 1252 (1972)(covenant which did not address scope, duration, and territory was unenforceable as a matter of law).

123 Idaho at 448-49, 848 P.2d at 390-91 (footnotes omitted).[5]

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[5] *McCandless* also discussed, with apparent approval, decisional law from outside Idaho including *Bryceland v. Northey*, 772 P.2d 36, 39 (Ariz.Ct.App.

(continued...)

Unlike the situation in many of the cited cases, there is no issue here as to the adequacy of consideration paid, the temporal term of restricted employment, nor the geographic scope of the excluded employment. The issue here concerns the prohibited "scope of activity."

The Restatement (Second) of Contracts, at §188(1)(a), provides that a promise to refrain from competition that imposes a restraint, which is ancillary to an otherwise valid transaction or relationship, is unreasonable if it is "greater than is needed to protect the promisee's legitimate interest." Such ancillary restraints include those of employees promising not to compete with their employers. Restatement (Second) of Contracts § 188(2)(b).[6]

The Idaho Supreme Court established in *Taylor* that, in addition to simply refusing to enforce a noncompetition agreement found to be unreasonably broad in time, territory or scope of prohibited activity, the court may also "modify" the agreement in exercise of its equitable powers. 94 Idaho at 899-900, 499 P.2d at 1255-56.

> It is the conclusion of this Court that the cases which authorize a modification of restrictive covenants ancillary to employment agreements are more consistent with the inherent concerns of a court of equity - fairness and reasonableness. Adoption of the

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[5](...continued)
1989), holding that restrictive covenants that tend to prevent an employee from pursuing a similar vocation after termination of employment are disfavored and will be strictly construed against the employer and that the employer bears the burden to prove the extent of its reasonably protectable interest, and *Hill v. Mobile Auto Trim, Inc.*, 725 S.W.2d 168, 170-71 (Tex. 1987), holding that such covenants, when applied to an employee's calling must satisfy four criteria in order to be found reasonable: (1) the covenant must be necessary for the protection of the promisee; (2) the covenant must not be oppressive to the promisor and in this respect the limitations as to time, territory and activity must be reasonable; (3) the covenant must not be injurious to the public; and (4) the promisee gives consideration for something of value.

[6] "A restraint may be ancillary to a relationship although, as in the case of an employment at will, no contract of employment is involved." Restatement (Second) of Contracts § 188, comment (g).

> modification principle allows a court to escape the rule of arbitrary refusal to enforce a covenant which, while unreasonable or indefinite in some of its terms, nevertheless serves to protect a legitimate interest of the parties or the public as the case may be. By rejecting the in toto approach and the 'divisibility' concept this Court seeks to provide flexibility to determining remedies available to the parties and the public. Consequently, enforcement is variable upon the circumstances of each case. Rather than choosing between absolute enforcement or unenforcement, there will be a wide range of alternatives available to meet the particular facts of the case being tried.

Id.[7]

DISCUSSION

There is no evidence supporting a violation of the Agreement insofar as it prohibits Wengert from directly or indirectly owning, managing, operating or controlling any fastener and tool business or any other business similar to K&R's. Nor is there evidence of a violation of the Agreement's prohibition upon divulging any of K&R's confidential or proprietary information or records, or of Wengert's contacting any past, present or future customers of K&R to attempt to entice them to leave.[8] Enforcement of the Agreement is

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[7] In *Taylor*, the covenant at issue "was so lacking in the essential terms which would protect the employee, namely a limitation on time, area, and scope of activity, that the covenant [was] as a matter of law unenforceable. The trial court did not modify the covenant - it had to supply the essential restrictions to make it reasonable." 94 Idaho at 900, 499 P.2d at 1256. As a result, even though the Idaho Supreme Court validated the principle of modification, it reversed the lower court.

[8] The Complaint specifically alleged that Wengert "has and will solicit Plaintiff's customers" and that he "is utilizing [K&R]'s practices, procedures, methods, trade secrets and techniques, customer lists, and other information, all in violation of the [Agreement]." K&R further alleged, "It appears likely that [Wengert] will induce, or attempt to induce [K&R]'s customers to terminate the services of [K&R] and rely on [Wengert] or other competitors of [K&R] to provide or facilitate the services now supplied by [K&R]." K&R also (continued...)

not supported on these grounds.

The crux of K&R's argument in support of preliminary injunction is that Wengert's employment violates the Agreement's prohibition upon his being "employed by . . . or . . . connected in any manner with the . . . management [or] operation . . . of any fastener and tool business or any other business presently or hereafter conducted by [K&R] similar to the type of business now or hereafter conducted by [K&R] in the [prohibited geographic area]."

K&R has taken the position that the "only trigger for the [Agreement] to apply is that the [new] business sell fasteners." Reply Brief at 7-8. K&R argues that a showing of actual competition is unnecessary and that the Agreement doesn't contemplate an analysis of the extent or magnitude of the competition existing or threatened by Wengert's future employers.[9] Yet, if the language of the Agreement was so strictly and uncritically applied, K&R would bar Wengert's employment but would achieve no correlative benefit since there is no existing or evident threat of competition by All-West. This Draconian approach gives K&R unnecessary relief at Wengert's expense (and at his

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[8](...continued)
alleged Wengert has converted to his own use K&R's customer lists. Complaint, paras. XVI, XVII, p.6. However, there was no evidence presented that Wengert has violated the Agreement in any of these regards nor evidence of any actual conduct of the type alleged. While the Court appreciates the concern which motivated K&R, it takes a dim view of K&R making categorical accusations without evident factual support. *Cf.* Rule 9011(b)(3) (submitting a complaint is a certification that, to the best of the attorney's knowledge "formed after an inquiry reasonable under the circumstances," the allegations have "evidentiary support.").

[9] The Court does not criticize K&R for asserting, in this litigation, a view of the Agreement using a strict or bright-line approach. All-West's filings with the Secretary of State and its placement of Yellow Pages advertising could give rise to legitimate concern over the possibility of competition. However, the facts presented do not bear out that concern. The Court has no doubt that K&R will be watching closely to determine if actual competition arises, notwithstanding the sworn testimony offered at the hearing. That testimony is likely to be quite relevant should prohibited competition occur within the eighteen month term of the Agreement (which commenced July 31, 1998 and expires January 31, 2000).

creditors' expense because he would not have the regular income from his employment with All-West to fund his plan). As held in *Hill*, the covenant must be necessary for the protection of the promisee, and not oppressive to the promisor. 725 S.W.2d at 170-71; *see also Taylor*, 94 Idaho at 899-900, 499 P.2d at 1255-56. The Agreement, if applied in a rigid, literal manner, meets neither standard. Such an approach to the Agreement also leads to violation of *Hill's* third element, that enforcement of the covenant must not be injurious to the public. *Id.*[10]

Even Terry Kowallis conceded that the Agreement was broader than necessary to safeguard K&R's interests. When he was questioned as to whether he believed the Agreement would prohibit Wengert from being employed by retailers such as Shopko or similar general merchandise/discount stores, or by home improvement outlets, or by traditional "hardware stores," he answered no. But all of these businesses sell, among other things, fasteners and tools and fall within the strict language of the Agreement. This testimony thus evinces that even K&R focuses on the nature and degree of competition in its understanding of the function to be served by the Agreement rather than on its literal terms.[11]

While the Agreement's prohibition may at first blush appear narrowly drawn,[12] the evidence establishes that it is broad enough to include businesses

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[10] *Accord*, *McCandless*, 123 Idaho at 448-49, 848 P.2d at 390-91 (the detriment to the public interest through the loss of the covenantee's services must be more than offset by the public benefit in preserving freedom of contract.)

[11] K&R's perception of what needed protection can be gleaned from its complaint which prays for relief enjoining Wengert from (a) soliciting, diverting or taking away K&R's customers, (b) directly or indirectly contacting or inducing K&R customers or clients to cease business with K&R or to do business with K&R's competitors, or (c) making use of customer lists, names or information. The record does not support relief on these grounds. The prayer also seeks an order enjoining Wengert from "violating any other portion of the covenants between [K&R] and [Wengert]"and it is solely because All-West falls within the "any fastener and tool business" rubric that the Agreement is allegedly violated.

[12] The language of the Agreement is not inherently unreasonable, but only (continued...)

posing no threat of competition. The restraint is therefore "greater than is needed to protect the promisee's legitimate interest." Restatement (Second) of Contracts § 188(1)(a). Alternatively stated, the Agreement is unreasonable in this regard because "it is greater than is required for the protection of the person for whose benefit the restraint is imposed or imposes undue hardship upon the person restricted." *Hill*, 725 S.W.2d at 170 (citations omitted).

As the authorities discussed above make clear, an unreasonable covenant is unenforceable. However, rather than denying enforcement in toto, the Court elects, as permitted by *Taylor*, to refuse enforcement only to the extent the same would be unreasonable.[13]

The Court, in evaluating the entirety of the record, finds and concludes that K&R has not established a basis for injunctive relief under the standards of *Barahona-Gomez*.[14]

K&R does not have a strong likelihood of success on the merits because the Court finds the blanket prohibition, which is the sole term of the Agreement violated by Wengert's employment at All-West, is unreasonable. K&R has not carried its burden to demonstrate that Wengert's employment by All-West invades its reasonably protectable interest. Nor does the evidence establish the possibility of irreparable injury to K&R in the absence of injunctive relief.

The Court does not find that the balance of hardships tilts in favor of K&R. K&R has not demonstrated that it is likely to suffer hardship if Wengert is allowed to continue his employment, whereas Wengert would clearly suffer undue hardship if he is prevented from continuing his employment and funding his chapter 13 plan.

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[12](...continued)
unreasonable in application under the record here developed.

[13] While *Taylor* allows the Court to modify the Agreement, the Court sees no particular value in attempting to redraft the language.

[14] Additionally, under *Drong*, injunction to enforce a covenant ancillary to an employment agreement should not be granted where, as here, the result would be inequitable.

CONCLUSION

Based upon the foregoing, K&R's Motion for Preliminary Injunction is DENIED. The Court's ruling will be without prejudice to renewal of the motion should future events support reconsideration of the matter.

DATED this 2nd of July, 1999.

TERRY L. MYERS
UNITED STATES BANKRUPTCY JUDGE